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No. 89-433

In the Supreme Court of the United States

OCTOBER TERM, 1989

DIRECTOR OF REVENUE, STATE OF MISSOURI,
Petitioner,

vs.

FREDERICK & JOSEPHINE HACKMAN,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF MISSOURI

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QUESTION PRESENTED

WHETHER FEDERAL PRINCIPLES OF RETROACTIVITY MUST BE APPLIED BY STATE COURTS IN DETERMINING THE RETROACTIVE/PROSPECTIVE APPLICATION OF THIS COURT'S OPINIONS?[1]

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1. As identical remedial issues are raised in *American Trucking Association v. Smith*, 746 S.W.2d 377 (Ark.) *cert. granted*, 109 S.Ct. 389, No. 88-325 (1988); *McKesson Corp. v. Division of Alcohol, Beverages & Tobacco*, 524 So.2d 1000 (Fla.) *cert. granted*, 109 S.Ct. 389, No. 88-192 (1988) (both cases were restored to the calendar for reargument), this petition is filed to protect Petitioner's interests and rights pending the Court's decision in those cases.

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No.

In the Supreme Court of the United States

OCTOBER TERM, 1989

DIRECTOR OF REVENUE, STATE OF MISSOURI,
Petitioner,

vs.

FREDERICK & JOSEPHINE HACKMAN,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF MISSOURI

OPINIONS BELOW

The Supreme Court of Missouri's final decree and opinion is reported at 771 S.W.2d 77 (App. A2).

The Missouri Administrative Hearing Commission's opinion has not been reported (App. A23).

The Final Decision of the Director of Revenue has not been reported (App. A30).

The Missouri Administrative Hearing Commission's opinion, on remand from Supreme Court of Missouri, has not been reported (App. A36).

JURISDICTIONAL STATEMENT

The Supreme Court of Missouri issued its Opinion on May 25, 1989. Petitioner's timely motion for rehearing was denied on June 15, 1989 (App. A1). Pursuant to 28 U.S.C. § 2101(c) and Supreme Court Rule 20, the present petition for a writ of certiorari is required to be filed within ninety days of the denial of rehearing.

Jurisdiction of this Court is invoked under 28 U.S.C. § 1257(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

1. U.S. Const. art IV, cl. 2:

> This constitution and the laws of the United States which shall be made in pursuance thereof, and all treaties made or which shall be made under the authority of the United States, shall be the supreme law of the land; and the judges in every state shall be bound thereby, anything in the constitution or laws of any state to the contrary notwithstanding.

2. 4 U.S.C. § 111:

> The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States, a territory or possession or political subdivision thereof, the government of the District of Columbia, or an agency or instrumentality of one or more of the foregoing, by a duly constituted taxing authority having juris-

diction, if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation.

3. Mo. Const. art I, § 13:

Ex post facto laws—impairment of contracts—irrevocable privileges. That no ex post facto law, nor law impairing the obligation of contracts, or retrospective in its operation, or making any irrevocable grant of special privileges or immunities, can be enacted.

4. Section 136.035.1, RSMo 1986:

The director of revenue from funds appropriated shall refund any overpayment or erroneous payment of any tax which the state is authorized to collect. The general assembly shall appropriate and set aside funds sufficient for the use of the director of revenue to make refunds authorized by this section or by final judgment of court.

5. Section 143.801.1, RSMo 1986:

A claim for credit or refund of any overpayment of any tax imposed by sections 143.011 to 143.996 shall be filed by the taxpayer within three years from the time the return was filed or two years from the time the tax was paid, whichever of such periods expires the later; or if no return was filed by the taxpayer, within two years from the time the tax was paid. No credit or refund shall be allowed or made after the expiration of the period of limitation prescribed in this subsection for the filing of a claim for credit or refund, unless a claim for credit or refund is filed by the taxpayer within such period.

STATEMENT OF THE CASE

On March 28, 1989, this Court struck down the Michigan Income Tax Act, § 206.30(1)(f) Mich. Comp. Laws Ann. (Supp. 1988), which exempted from taxation retirement benefits paid by the state or its political subdivisions, but taxed retirement benefits paid by other employers, including the Federal government, as violative of the principles of intergovernmental tax immunity and 4 U.S.C. § 111. *Davis v. Michigan Department of Treasury*, ... U.S. ....., 109 S.Ct. 1500 (1989). *Hackman v. Director of Revenue*, 771 S.W.2d 77 (Mo. banc 1989) concerns the retroactive or prospective effect of the *Davis* decision on the Missouri income tax laws which are materially similar to the Michigan Income Tax Act.

The State of Missouri exempted most state and local pensions from state income tax. The retirement benefits of all other employees, including Federal government employees, were subject to Missouri income tax to the extent included in Federal adjusted gross income.

Respondents Frederick and Josephine Hackman duly paid their Missouri individual income tax for the years 1985 through 1988 inclusive. In calculating their Missouri adjusted gross income for these years, Respondents began with their Federal adjusted gross income. Included in their Federal adjusted gross income were pension benefits that Mr. Hackman received from the United States Government for prior military service.

Based on the *Davis* decision, Respondents, on April 24, 1989, filed refund claims with Petitioner for their 1985 through 1988 tax years. An agent of Petitioner denied Respondents' claims for refund. Respondents protested

the agent's denial to Petitioner and Petitioner issued his Final Decision sustaining the denial of Respondents' refund claims (App. A30).

Respondents appealed Petitioner's Final Decision to the Missouri Administrative Hearing Commission. On May 1, 1989, the Missouri Administrative Hearing Commission sustained the Petitioner's Final Decision denying the refunds (App. A23).

Respondents appealed the Missouri Administrative Hearing Commission's decision to the Supreme Court of Missouri. Petitioner cross-appealed an evidentiary ruling of the Missouri Administrative Hearing Commission (App. A24) to the Supreme Court of Missouri. The two appeals were consolidated.

On May 25, 1989, the Supreme Court of Missouri, en banc, held that based on this Court's decision in *Davis*, Missouri's practice of exempting most state and local pensions from Missouri income tax, while taxing Federal pensions, violated the doctrine of intergovernmental tax immunity (App. A6). Without deciding the retroactive/prospective application of *Davis* argued by Petitioner, the Supreme Court of Missouri further held that Missouri statutory and case law required refunds of unconstitutionally collected taxes (App. A9). The Court reversed the decision of the Missouri Administrative Hearing Commission and remanded the case back to the Commission for further proceedings (App. A13). On June 15, 1989, the Supreme Court of Missouri entered an order (without opinion) denying Petitioner's timely Motion for Rehearing (App. A1).

On remand, the Missouri Administrative Hearing Commission issued its opinion, in accordance with the

Missouri Supreme Court's decision in *Hackman v. Director of Revenue*, 771 S.W.2d 77 (Mo. banc 1989), granting Respondents' refunds (App. A36).

REASONS FOR GRANTING THE PETITION

THE SUPREME COURT OF MISSOURI MISCONSTRUED OR OVERLOOKED DISPOSITIVE FEDERAL AUTHORITY REQUIRING THE APPLICATION OF FEDERAL PRINCIPLES OF RETROACTIVITY TO DETERMINE THE RETROACTIVE/PROSPECTIVE APPLICATION OF THIS COURT'S DECISION IN DAVIS V. MICHIGAN DEPARTMENT OF TREASURY, ... U.S. ....., 109 S.CT. 1500 (1989).

Based on this Court's decision in *Davis v. Michigan Department of Treasury*, ... U.S. ....., 109 S.Ct. 1500 (1989), the Supreme Court of Missouri declared the Missouri income tax scheme in question unconstitutional (App. A6), and ordered refunds without any analysis of whether *Davis* should be applied retroactively under the three-factor test found in *Chevron Oil Co. v. Huson*, 404 U.S. 97, 30 L.Ed.2d 296, 92 S.Ct. 349 (1971) (App. A9). By failing to address the retroactive/prospective issue, the Supreme Court of Missouri misconstrued or overlooked Federal authority requiring an analysis of the retroactive/prospective issue. Further, the Supreme Court of Missouri's failure to apply *Chevron* to determine the retroactive/prospective effect of *Davis* raises remedial issues identical to those raised in the following two cases argued before this Court last term: *American Trucking Association v. Smith*, 746 S.W.2d 377 (Ark.) *cert. granted*, 109 S.Ct. 389, No. 88-325 (1988); *McKesson*

Corp. v. Division of Alcohol, Beverages & Tobacco, 524 So.2d 1000 (Fla.) *cert. granted*, 109 S.Ct. 389, No. 88-192 (1988).

Both cases were restored to the calendar for reargument. This petition is filed to protect Petitioner's interests and rights pending the Court's decision in *American Trucking* and *McKesson*.

Based upon the briefs filed by the parties and numerous amici curiae and the oral arguments presented to this Court, it is clear that *American Trucking Association* and *McKesson* will explain the proper analysis to employ when determining whether a refund is owed for taxes collected under a state tax statute declared unconstitutional under Federal law. In particular, both cases will by necessity determine the appropriate application of the *Chevron* analysis in such situations. Twenty-one states (App. A19 and A20) may be affected by the *Davis* decision; therefore, these remedial issues "cry out for clarification by the Court." Tatarowicz, *Right to a Refund for Unconstitutionally Discriminatory State Taxes and Other Controversial State Tax Issues Under the Commerce Clause*, 41 Tax Law. 103, 141 (1987).

When Federal rights are not implicated, the Constitution does not require the use of Federal prospectivity standards, and the individual states are free to determine retroactivity. *Great Northern Railway Co. v. Sunburst Oil Refining Co.*, 287 U.S. 358, 77 L.Ed. 360, 53 S.Ct. 145 (1932). However, in cases involving enforcement of rights under Federal law or the Federal Constitution, the Federal standards of prospectivity as enunciated in *Chevron* should be applied. *See, Tatarowicz, supra*, at 140.

Although Federal rights are involved in this case, the Supreme Court of Missouri failed to apply Federal prospectivity standards to determine whether *Davis* should be given retroactive or prospective effect in Missouri. The Missouri Court stated:

> Before reaching the issue of retroactive/prospective application, however, a threshold inquiry is necessary. "In order to reach the retroactivity issue, this court must first decide if . . . state statutory law or state case law mandates refunds of taxes paid prior to the Supreme Court's . . . decision. If this state's tax refund statutes . . . apply, then all other issues are irrelevant." *National Can Corp. v. Department of Revenue*, 109 Wash.2d 878, 749 P.2d 1286, 1287 (1988).

(App. A7).

Having initially concluded that state law controlled, the Supreme Court of Missouri then concluded that Missouri statutory and case law mandated such refunds. Thus, the court made no analysis of the retroactive/prospective issue under Federal law as required by the Supremacy Clause of the United States Constitution as contained in Article IV, clause 2, and *Chevron Oil Co. v. Huson*, 404 U.S. 97 (1971) (App. A9).

As a result, the Supreme Court of Missouri misconstrued or overlooked dispositive Federal authority which requires an initial analysis of the retroactive/prospective issue. The Supreme Court of Missouri first decided, as all parties had conceded, that Missouri's system of taxing Federal retirement benefits while exempt-

ing state retirement benefits from taxation "violates principles of intergovernmental tax immunity . . . ." (App. A6). Those principles are founded upon the United States Constitution, *See, McCulloch v. Maryland,* 17 U.S. (4 Wheat.) 316 (1819), and upon Federal statutory law. 4 U.S.C. § 111 (1985). Further, the Missouri Supreme Court's holding was founded upon this Court's holding in *Davis v. Michigan Department of Treasury,* ..... U.S. ....., 109 S.Ct. 1500 (1989). Thus, the Missouri Supreme Court's initial holding, that the Missouri tax scheme in question was unconstitutional, was based exclusively upon principles of Federal law.

"Where a state statute is held to violate the Federal Constitution, the retroactivity *vel non* of that holding is similarly a matter of Federal law which [the Court] must determine independently." *Cohn v. G.D. Searle,* 784 F.2d 460, 463 (3rd Cir. 1985); *Love v. Johns-Manville Canada, Inc.,* 609 F.Supp. 1457, 1460 (D.N.J. 1985) ("[I]t would be somewhat anomalous to countenance a rule which would leave states free to implement or delay implementation of Federal constitutional rulings on state law decisional grounds.")

The *Cohn* and *Love* decisions, as well as the Supremacy Clause of the United States Constitution, require that Federal law be examined initially to determine whether the *Davis* decision should be applied retroactively or prospectively. Because Federal law should control, Petitioner respectfully submits that the Supreme Court of Missouri overlooked or misconstrued the applicable Federal law by deciding the retroactive/prospective application of Federal constitutional rights based solely on state law.

A. Foreseeability of the Davis v. Michigan Department of Treasury, ... U.S. ....., 109 S.Ct. 1500 (1989) Decision.

An examination of the three factors enunciated in *Chevron*, reveals that *Davis* should have been given prospective effect by the Supreme Court of Missouri.

Chevron states:

> First, the decision to be applied nonretroactively must establish a new principle of law, either by overruling clear past precedent on which litigants may have relied or by deciding an issue of first impression whose resolution was not clearly foreshadowed. Second, it has been stressed that "we must . . . weigh the merits and demerits in each case by looking to the prior history of the rule in question, its purpose and effect, and whether retrospective operation will further or retard its operation." Finally, we have weighed the inequity imposed by retroactive application for "[w]here a decision of this Court could produce substantial inequitable results if applied retroactively, there is ample basis in our cases for avoiding the 'injustice or hardship' by a holding of nonretroactivity."

404 U.S. at 106-07 (citations omitted).

As "*Davis* represents both a new principle of law and a case of first impression" (App. A21, Welliver, J., dissenting), the first *Chevron* factor is easily met in this case. At least twenty-one states granted state income tax exemptions for retirement benefits of state and local employees which they did not grant to Federal employees (App. A20, n.2); *see also Davis*, 109 S.Ct. at 1511, n.3.

(Stevens, J., dissenting). Missouri state and local pension statutes have provided state income tax exemptions since 1929. *See, e.g.*, the police pension law amendments (currently in § 86.190, RSMo 1986). Missouri has also adopted additional exemptions from time to time, and most after the enactment in 1939 of 4 U.S.C. § 111. However, Petitioner has found no court decision, state or Federal, which invalidated any such exemptions prior to this Court's decision in *Davis*. Indeed, the dissent in *Davis* notes that the cases cited by the majority of the Court are "significantly different." *Davis*, 109 S.Ct. 1512. (Stevens, J., dissenting).

Furthermore, the states could not have foreseen the result in *Davis*. Those cases which had addressed discrimination against Federal pensioners in a tax context uniformly upheld the validity of exempting state pension benefits from state taxation even though Federal pension benefits were not exempt.[2] Certainly, the Michigan decisions which preceded *Davis* gave no indication that the Michigan statute would be declared unconstitutional.

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2. *See, e.g., In the Matter of the Petition of Walter C. Yurkus*, New York State Tax Commission No. TSB-H-82(371)-I, December 31, 1982 (State income tax can be collected on Federal pensions even though not due on state pensions); *In the Matter of the Petition of Israel Resnick and Sadie Resnick*, New York State Tax Commission No. TSB-H-84(25)-I, February 23, 1984 (State income tax can be collected on Federal pensions even though not due on state pensions); *Butzback v. Director Division of Taxation*, 3 N.J. Tax 462 (N.J. Tax Ct. 1981) (State inheritance tax may be imposed on transfer of Federal annuity even though state annuity transfer is exempt from same tax); *see also Gritzmacker v. Director, Division of Taxation*, 2 N.J. Tax 489 (N.J. Tax Ct. 1981) (same result for private versus state pensions); *Huckaba v. Johnson*, 573 P.2d 305 (Or. 1977) (State may discriminate in imposing state income tax on some Federal pensions as opposed to state pensions and other Federal pensions). These long-standing, valid statutes and decisions constitute a base of law upon which Petitioner justifiably relied and as to which *Davis* created new law.

Davis v. Dept. of Treasury, No. 84-9541 (Ct. Claims 1985); *Davis v. Dept. of Treasury*, 160 Mich. App. 98, 408 N.W.2d 433 (1987); and *Davis v. Dept. of Treasury*, 429 Mich. 854 (1987). Further, Justice Stevens noted in his dissent that "[t]he Court's holding is not supported by the rationale for the intergovernmental immunity doctrine and is not compelled by our previous decisions." *Davis*, 109 S.Ct. at 1509. As the Supreme Court of Oklahoma noted in *First of McAlester Corp. v. Okl. Tax Com'n*, 709 P.2d 1026, 1034 (Okl. S.Ct. 1985), "[i]t is equally persuasive that the type of . . . tax in question might reasonably have been assumed to be constitutional based on the longstanding and widespread practice of various states to which the United States Supreme Court has not specifically spoken."

Davis established a new principle of law and decided an issue which was not foreshadowed within the meaning of the first *Chevron* factor. As such, retroactive application of *Davis* would upset the justified expectations of Missouri and her sister states in the presumptive constitutional validity of their taxing schemes. The first *Chevron* factor clearly supports prospective application of *Davis*.

B. Purposes of Intergovernmental Tax Immunity and Retroactivity Application of Davis v. Michigan Department of Treasury, ... U.S. ....., 109 S.Ct. 1500 (1989).

The second *Chevron* factor is to "weigh the merits and demerits in each case by looking to the prior history of the rule in question, its purpose and effect, and whether retrospective operation will further or retard its operation." *Chevron*, 404 U.S. at 106-07. At issue in *Davis* was the relationship between the state and Federal governments. Respondents' request for a refund in this case

did not affect the relationship between the state and Federal governments and thus presented no reason for retroactive application of *Davis*. Retroactive application of *Davis* would require Missouri to issue refunds to Federal pensioners. A requirement that Missouri issue refunds to Federal pensioners, coupled with the state's inability to retroactively tax its state pensioners, Mo. Const. art I, § 13, would impose a substantial penalty on the state and its taxpayers without furthering the purposes behind the intergovernmental tax immunity doctrine.

In *Graves v. New York*, 306 U.S. 466, 83 L.Ed. 927, 59 S.Ct. 595 (1939), this Court explained that the theory of tax immunity rests on an implied limitation of the Federal and state governments' taxing powers: the purpose of the rule is to avoid interference with the functions of the taxed government through the exercise of that power by the other. *Graves*, 306 U.S. at 477-78, 480. "[T]he only possible basis for implying a constitutional immunity from state income tax of the salary of an employee of the national government or of a governmental agency is that the economic burden of the tax is in some way passed on so as to impose a burden on the national government tantamount to an interference by one government with the other in the performance of its functions." *Id.* at 481; *See also, Detroit v. Murray Corp.*, 355 U.S. 489, 504, 2 L.Ed.2d 460, 465, 78 S.Ct. 486, 491 (1958) (Frankfurter, J., dissenting). ("It is in avoiding the potentialities of friction and furthering the smooth operation of complicated governmental machinery that the constitutional doctrine of immunity finds its explanation and justification.")

For a private citizen to claim the protection of such immunity, he must show that benefiting the citizen at the

expense of the taxing sovereign somehow reduces the state-federal tension. Even though this Court recognized in *Davis* that private parties subjected to discriminatory taxation may be entitled to the protection of intergovernmental immunity, "where that immunity is invoked by the private citizen it tends to operate for his benefit at the expense of the taxing government and without corresponding benefit to the government in whose name the immunity is claimed." *Graves*, 306 U.S. at 483. Such is this case. A retroactive application in this case would place an onerous burden upon the State of Missouri without in any way advancing the doctrine of intergovernmental tax immunity. Thus, the second *Chevron* factor also favors prospective application of *Davis*.

C. Equities Favor Prospective Application of Davis v. Michigan Department of Treasury, ... U.S. ....., 109 S.Ct. 1500 (1989).

The third factor of *Chevron* is to weigh the inequities imposed by retroactive application. 404 U.S. 107. Equitable considerations in this case support prospective application of *Davis*.

A retroactive application of *Davis* and the consequential refunds to Federal pensioners would create difficult hardships for the State of Missouri, its political subdivisions and taxpayers.[3] This Court recognizing the reality of these hardships, has often held civil legislation unconstitutional, yet given only prospective effect to its holding, in order to avoid imposing undue administrative or financial burdens on agencies or local governments. *See, e.g.*,

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3. Estimated total revenue loss from retroactive application of *Davis* (including refunds) will be approximately $192 million in fiscal year 1990.

Lemon v. Kurtzman, 411 U.S. 192, 36 L.Ed.2d 151, 93 S.Ct. 1463 (1973); *Cipriano v. City of Houma*, 395 U.S. 701, 23 L.Ed.2d 647, 89 S.Ct. 1897 (1969); *cf. Great Northern Railway Co. v. Sunburst Oil Refining Co.*, 287 U.S. 358, 77 L.Ed. 360, 53 S.Ct. 145 (1932).

Similarly, state courts have given holdings invalidating taxes or assessment procedures only prospective effect due to the severe hardships that would be created by retroactive application. *See, e.g., Ashland Oil, Inc. v. Rose*, 350 S.E.2d 531 (W. Va. 1986) *app. dismissed*, 107 S.Ct. 1949 (1987); *Salorio v. Glaser*, 461 A.2d 1100 (N.J. 1983) *cert. denied*, 464 U.S. 993, 78 L.Ed.2d 682, 104 S.Ct. 486 (1983); *Metropolitan Life Ins. Co. v. Com'r of Dept. of Ins.*, 373 N.W.2d 399 (N.D. 1985); *First of McAlester Corp. v. Oklahoma Tax Com'n*, 709 P.2d 1026 (Okl. S.Ct. 1985).

Furthermore, Missouri has for many years relied on its ability to generate revenue from the income tax on Federal and other pensions. This Court acknowledged this type of reliance in *Lemon v. Kurtzman, supra*, "statutory or even judge-made rules of law are hard facts on which people must rely in making decisions and in shaping their conduct. This fact of legal life underpins our modern decisions recognizing a doctrine of nonretroactivity." *Id.* at 199. Similarly, in *Ashland Oil, Inc. v. Rose, supra*, at 537, the West Virginia Court stated: "[w]e believe, therefore, that the reliance of the State of West Virginia on a presumptively valid tax outweighs any injury that may be sustained by Ashland on account of our holding of prospectivity."

"It is well established that reliance interests weigh heavily in the shaping of an appropriate equitable remedy." *Lemon v. Kurtzman*, 411 U.S. at 203. The expenditures made by the State of Missouri from the revenue

raised by taxing Federal pensions cannot be undone, and reimbursement at this point would impose a significant hardship upon Missouri's existing financial requirements. *See, Metropolitan Life v. Com'r, supra,* at 412; *Salorio v. Glaser, supra.* The appropriate remedy in this case is a prospective application of *Davis.*

CONCLUSION

The petition for a writ of certiorari should be granted pending this Court's decision in *American Trucking* and *McKesson.*

Respectfully submitted,

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September, 1989

APPENDIX

(Dated June 15, 1989)

SUPREME COURT OF MISSOURI
EN BANC

June 15, 1989

ORDERS

71628 Frederick & Josephine Hackman, appellants/cross-respondent vs. Director of Revenue, State of Missouri, respondent/cross-appellant.

Respondent/Cross-Appellant's motion for rehearing overruled.

71756 In re: The Hon. L. Thomas Elliston, resp.

Commission on Retirement, Removal & Discipline's motion to disqualify overruled.

Day - to - Day

/s/ William H. Billings
William H. Billings, Chief Justice

(Filed May 25, 1989)

SUPREME COURT OF MISSOURI
EN BANC

No. 71628

FREDERICK & JOSEPHINE HACKMAN,
Appellants/Cross-Respondents,

v.

DIRECTOR OF REVENUE,
STATE OF MISSOURI,
Respondent/Cross-Appellant.

PETITION FOR REVIEW OF A DECISION OF THE ADMINISTRATIVE HEARING COMMISSION
Honorable Paul M. Spinden

On March 28, 1989, the United States Supreme Court decided *Davis v. Michigan Department of Treasury*, ... U.S. ....., 57 U.S.L.W. 4389 (1989). *Davis* held that Michigan's income taxation scheme, which exempted from taxation all retirement benefits paid by the state or its political subdivisions but levied an income tax on retirement benefits paid retired federal employees, violated 4 U.S.C. § 111.[1]

In this case we face two issues: First, whether Missouri's exemption from income taxation of certain retire-

1. 4 U.S.C. § 111 provides:

The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States . . . by a constituted taxing authority having jurisdiction, *if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation.* [Emphasis added.]

ment benefits paid public employees and Missouri's concomitant failure to exempt pensions of federal retirees likewise violate principles of intergovernmental tax immunity; second, if Missouri's income taxation scheme is illegal under *Davis*, whether, and under what circumstances, federal retirees who paid the discriminatory tax may recover a refund. This case involves the construction of the revenue laws of this state. We have jurisdiction. Mo. Const. art. V, § 3.

We hold that under the teachings of *Davis* Missouri's income tax scheme violates principles of intergovernmental tax immunity. We further hold that appellants herein are entitled to a refund to the extent that such refund is permitted by Section 143.801, RSMo 1986. Reversed and remanded for such further proceedings consistent with this opinion.

I.

Appellants Frederick and Josephine Hackman filed combined Missouri income tax returns for the years 1985 through 1988, inclusive. Included in the Hackmans' income for purposes of the Missouri income tax return were Mr. Hackman's military retirement benefits paid by the United States government. Following the announcement of the United States Supreme Court's decision in *Davis*, appellants filed claims for refund with the Director of Revenue (the Director) pursuant to Section 143.801, RSMo 1986, for tax years 1985 through 1988. As a basis for their refund claims, appellants argued that taxes paid on the federal military retirement benefits were overpayments.

On April 24, 1989, the Department of Revenue denied appellants' claims for refund. Likewise on April 24, 1989, appellants filed a timely protest of that denial, pursuant

to Section 143.841, RSMo 1986. The Director denied the protest that same day.

Appellants sought review of the Director's final decision with the Administrative Hearing Commission (the Commission) pursuant to Section 621.050, RSMo 1986. The parties waived hearing and submitted the case on stipulated facts. On May 1, 1989, the Commission held that it was without jurisdiction to determine appellants' claims for refund. *City of Joplin v. Industrial Commission of Missouri,* 329 S.W.2d 687 (Mo. banc 1959); *State Tax Commission v. Administrative Hearing Commission,* 641 S.W.2d 69 (Mo. banc 1982). The Commission therefore dismissed appellants' complaint; the effect of that dismissal was to sustain the Director's decision denying the refunds. This petition for review followed.

II.

The Director of Revenue, amici curiae and appellants concede that Missouri's taxation scheme offends 4 U.S.C. § 111 under *Davis.* That concession is well-founded. We are aware of but three distinctions between Michigan law and Missouri law, none of which compels a contrary result.

First, § 206.30(1)(f) Mich. Comp. Laws Ann. (Supp. 1988), provides in pertinent part:

> (1) "Taxable income" . . . means adjusted gross income as defined in the internal revenue code subject to the following adjustments;
>
> * * *
>
> (i) Retirement or pension benefits received from a public retirement system of or created by an act of this state or a political subdivision of this state.
>
> * * *

(iv) Retirement or pension benefits from any other retirement or pension system as follows:

(A) For a single return, the sum of not more than $7,500.00.

(B) For a joint return, the sum of not more than $10,000.00.

Unlike Michigan, exemptions for state public retirement benefits from income taxation under Missouri law are not found in the taxing statutes. Instead, our legislature provides the income tax exemptions in the statutes that create the various retirement systems. *See, e.g.*, Section 70.775 RSMo 1986 (pensions for officers and employees of political subdivisions); Sections 86.190, 86.353, 86.493 and 87.365, RSMo 1986 (police and fire pensions); Section 104.250 RSMo 1986 (pensions of former employees of the State Highway Patrol and former employees of the Department of Highways and Transportation); Section 104.540 RSMo 1986 (pensions of former elected state officials and state merit system employees); and Section 169.587 RSMo 1986 (pensions of former teachers and school employees). The effect of Missouri's scattered retirement benefit exemption statutes is identical to that of Michigan's exemption statute for purposes of a *Davis* analysis.

Second, *Davis* involved a federal civil service employee's retirement benefit; appellants receive a federal military pension. 4 U.S.C. § 111 draws no distinction between federal military personnel and civil service personnel; nor shall we draw such a distinction.

Third, Section 206.30 (1)(f)(iv) expressly exempts $7,500 in retirement benefits for a single return and $10,000 for a joint return from any pension for purposes of income taxation. For the years in question, Missouri pro-

vided no such exemption for benefits received under non-state retirement plans. To the extent that Michigan permitted some exemption for federal retirees, its taxation scheme is arguably more favorable to federal retirees, than is Missouri's. Nevertheless, *Davis* finds Michigan's plan violative of 4 U.S.C. § 111. We are confident that *Davis* mandates a similar condemnation of Missouri law.

We hold, as the parties concede, that Missouri's system of taxation, which exempts the receipt of public retirement benefits for purposes of Missouri income taxation, "violates principles of intergovernmental tax immunity by favoring retired state and local government employees over retired federal employees." *Davis*, ... U.S. at ....., 57 U.S.L.W. at 4393.

III.

The United States Supreme Court did not announce whether its decision in *Davis* had retrospective or prospective application, perhaps in large measure because Michigan conceded[2] that "to the extent appellant has paid taxes pursuant to this invalid tax scheme, he is entitled to a refund." ..... U.S. at ....., 57 U.S.L.W. at 4393. In light of this uncertainty, the Director argues that we should apply the test announced in *Chevron Oil Co. v. Huson*, 404 U.S. 97 (1971), and adopted by this Court in *Sumners v. Sumners*, 701 S.W.2d 720 (Mo. banc 1985). By application of that test, the Director contends, *Davis*

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2. Section 206.441, Mich. Comp. Laws Annot., provides:

> A taxpayer who has paid a tax which he or she claims was not due under this act may, on or before the expiration of 4 years from the date set for the filing of the annual or final return for the year or the date the tax was paid, whichever is later, and not after, petition the commissioner in writing to refund the amount paid.

need only be applied prospectively and appellants would not be entitled to a refund.

Before reaching the issue of retroactive/prospective application, however, a threshold inquiry is necessary. "In order to reach the retroactivity issue, this court must first decide if . . . *state statutory law or state case law* mandates refunds of taxes paid prior to the Supreme Court's . . . decision. If this state's tax refund statutes . . . apply, then all other issues are irrelevant." *National Can Corp. v. Dept. of Revenue*, 109 Wash.2d 878, 749 P.2d 1286, 1287 (1988) (emphasis added).

> The General Assembly has required that the Director: from funds appropriated shall refund any overpayment or erroneous payment of any tax which the state is authorized to collect. The general assembly shall appropriate and set aside funds sufficient for the use of the director of revenue to make refunds authorized by this section or by final judgment of court.

Section 136.035.1, RSMo 1986. In addition, the legislature has prescribed a specific procedure by which persons who seek an income tax refund can obtain it.

> A claim for credit or refund of an overpayment of any tax imposed by section 143.011 to 143.996 shall be filed by the taxpayer within three years from the time the return was filed or two years from the time the tax was paid, whichever of such periods expires the later; . . . . No credit or refund shall be allowed or made after the expiration of the period of limitation prescribed in this subsection for the filing of a claim for credit or refund, unless a claim for credit or refund is filed by the taxpayer within such period.

Section 143.801.1, RSMo 1986. The statute presents two requirements for securing a refund: (1) a claim based on an overpayment (2) filed within three years of the filing of the return or two years of the payment of the tax. Both requirements must be met or no credit or refund is available to the taxpayer.

As to the first requirement, this Court has previously defined the word "overpayment" for purposes of Section 143.801 in *Homestake Lead v. Director of Revenue*, 759 S.W.2d 847 (Mo. banc 1988). Relying on *Community Federal Savings & Loan Assoc. v. Director of Revenue*, 752 S.W.2d 794, 798 (Mo. banc 1988), we held that "payment of a tax which was wholly unauthorized by law was an 'overpayment.'" *Homestake Lead*, 759 S.W.2d at 848. The Court reasoned that:

> Unlike some tax refund statutes (e.g., § 139.031, RSMo 1986), § 143.801 does not require payment under protest as a condition of filing a claim for refund. The general assembly, just as the federal congress, apparently thought that the intricacies of income taxation were such *that means for* correcting inadvertencies or *responding to intervening* [court] *decisions should be provided.*

Id. at 849. [Emphasis added.]

Homestake Lead is not an aberration. This Court has consistently held that the word "overpayment" includes taxes illegally collected in other contexts. *See Kleban v. Morris*, 247 S.W.2d 832, 839 (Mo. 1952) ("The word 'overpayment' in Section 144.190 [sales tax] includes taxes 'illegally collected' . . . .") and *Community Federal*, 752 S.W.2d at 798, ("a reasonable construction of the terms 'overpayment' and 'erroneous' as used in section 136.035 [RSMo 1986] includes the term 'illegal' . . . .").

We see no valid reason to alter the definition of "overpayment" adopted by this Court for purposes of tax refund statutes. The legislature is presumed to be aware of interpretations placed on these statutes by this Court in *Kleban, Hern v. Carpenter,* 312 S.W.2d 823, 828 (Mo. 1958), *Community Federal* and *Homestake Lead. Martin v. Mid-America Farm Lines Inc.,* ..... S.W.2d ....., ... (Mo. banc 1989) (No. 70857, decided April 16, 1989) (slip op. at 12); *Person v. Scullin Steel Co.,* 523 S.W.2d 801, 803 (Mo. banc 1975); *Messick v. Gringer,* 205 S.W.2d 739, 741-2 (Mo. 1947). Despite this presumed knowledge, the General Assembly has not passed legislation requiring a contrary result.

By its adoption of Section 136.035, we have held that the State has "consented to a refund of any overpayment, erroneous or illegal payment, which would include a tax declared unconstitutional. . . ." *Community Federal,* 752 S.W.2d at 798. For the reasons expressed in *Community Federal* and *Homestake Lead,* we hold that by its adoption of Section 143.801, the State of Missouri has consented to a refund of any overpayment, erroneous payment or illegal payment of income tax. And, as we have said, an overpayment includes those income taxes collected illegally under a taxation scheme which violates principles of intergovernmental tax immunity. *Davis,* ..... U.S. at ....., 57 U.S.L.W. at 4393. If appellants meet the procedural requirements of Section 143.801, they are entitled to a refund under the mandate of the statute as interpreted by the decisions of this Court previously cited. Having so concluded, there is no need to consider whether *Davis* should be applied retroactively or only prospectively; the Director's point is, therefore, denied.

The record before this Court does not show when appellants filed their 1985 tax return. Nor does the record reveal whether appellants filed their claim for refund for tax year 1985 "within three years from the time the return was filed . . . ." Section 143.810.1. We are not favored by arguments of the parties as to whether the language of Section 143.810.1 requires filing a claim for refund within three years of the actual filing of the return, as the plain language of the statute seems to indicate, or whether the Director has interpreted the phrase, as we understand the Internal Revenue Service interprets a similar phrase in the federal tax code, to mean that tax returns are filed for purposes of a refund on April 15, no matter if the taxpayer sends the return in earlier. These lacunae prevent this Court from determining whether appellants are entitled to a refund for their 1985 tax year. On remand the Commission will be required to address this question.

IV.

The Director argues that he "may not make refunds of the magnitude which a retroactive application of the *Davis* opinion would necessitate without an appropriation by the general Assembly." The point is without merit.

This case involves a total claim for refund of $2,317;[3] only that amount is at issue in this case. We are not, of course, deaf to the public pronouncements that the precedent established by this case bears a potential

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3 Appellants claim for refund is as follows:

1985	$498
1986	$669
1987	$614
1988	$536

$150,000,000+ cost for the State. Nevertheless, whether the State has appropriated the funds necessary is not relevant to our consideration of the merits of appellants' claims in this case. The role of the judicial branch under these circumstances is "to adjudicate whether the State is obligated . . . . It remains for the General Assembly to appropriate the money if it be determined that the State is so obligated." *V. S. DiCarlo Const. Co., Inc. v. State*, 485 S.W.2d 52, 57 (Mo. 1972).

We have no reason to believe that the General Assembly will fail to recognize the State's obligations and take appropriate action to meet those obligations in a manner consistent with its own directive, found in Section 136.035.1, to appropriate funds required to pay for refunds of overpayment or erroneous payment of taxes.[4]

V.

Amicus curiae Griffin and Mathewson argue in the alternative that if this Court finds that *Davis* is not to be applied prospectively in this case, we must nevertheless

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4. We take judicial notice that the General Assembly appropriated and the Governor approved $228,800,000E "To the Department of Revenue: For the purpose of paying refunds for overpayment or erroneous payment of any tax or any payment which is credited to the General Revenue Fund". § 4.080, H.B. 4, (85th General Assembly, First Regular Session). We also take judicial notice that the State of Missouri, Comprehensive Annual Financial Report for the Fiscal Year ended June 30, 1988, provides in its Notes to the Financial Statements of June 30, 1988, a description of the state's system of budgetary accounting and there explains the purpose of the "E" following the appropriation. "Certain estimated original appropriation amounts *may be increased as necessary.*" (Emphasis added.) Such open-ended appropriations with estimated amounts do not constitute maximum limitations. Op. Atty. Gen. No. 56, Spainhower, (March 19, 1976). It appears, though we do not decide the point, that the General Assembly has appropriated funds for all refunds for overpayment or erroneous payments of taxes in § 4.080, including those which may be required under *Davis*.

affirm the Commission's decision. These amici urge that the appropriate remedy is to tax Missouri retirement benefits rather than grant refunds to federal retirees. Amici suggest that we remand the case to the Commission "with directions to give no effect to the pension benefit exemption statutes at issue." In support, amici cite *Linnane v. Clark*, ... A.2d ..... (R.I. 1989) (Nos. 87-478-M.P. & 88-192-M.P., decided April 19, 1989), a case in which the Rhode Island Supreme Court held that its state income tax, which included state and local pension benefits in taxable income, controlled over exemption provisions in its retirement laws.

We reject this argument. First, in *Linnane*, the Rhode Island Supreme Court found that Rhode Island's pension exemption statute had been repealed by implication with the passage of the state's income tax statute. The court reasoned that because the pension exemption statute was a statute of general application, had been adopted in 1956 and appeared in a different chapter of the code, the more specific income tax statute enacted in 1971 effected its repeal.

Our income tax statutes, Sections 143.011, *et seq.*, were effective January 1, 1973. As we have previously noted, Missouri's pension exemption statutes are found in the statutes creating the pensions and not in the income tax statutes. Section 70.775 was passed in 1967; Section 86.190 was passed in 1939; Section 86.353 was passed in 1957 and amended in 1961; Section 86.493 was passed in 1945 and amended in 1985; Section 87.365 was passed in 1943 and amended in 1959; Section 104.250 was passed in 1955 and amended in 1983; Section 104.540 was passed in 1957 and amended in 1981; and Section 169.587 was passed in 1976.

Repeals by implication are not favored in Missouri. "[F]or repeal of a statute by implication, the statutes must be so inimical to each other that both cannot stand

and the legislature, in fact, intended repeal although it did not do so." *Bartley v. Special School District of St. Louis County,* 649 S.W.2d 864, 867 (Mo. banc 1983). That the legislature did not intend to repeal these pension exemption statutes by implication is seen in the General Assembly's attention to several of the exemption statutes after the effective date of the income tax statute.

Second, on May 12, 1989, the General Assembly passed and sent to the Governor H.B. 674, which taxes public employee retirement benefits in Missouri for future tax years. A decision by this Court which reaches the same result would be an act devoid of meaning.

Third, we believe the fashioning of a remedy to deal with the fiscal strain anticipated by the application of *Davis* to appellants' claim for refund is a matter reserved to the legislative branch under our constitution. Just as we refuse to adopt the arguments of amici suggesting that we determine that the exemptions heretofore honored under our law for state and local retirees be held for naught, we reject any suggestion that this Court should inject itself into matters more ably, and properly, determined by the legislature.

VI.

The decision of the Administrative Hearing Commission is reversed and the cause remanded for further proceedings consistent with this opinion.

Edward D. Robertson, Jr., Judge

Billings, C.J., Blackmar, Higgins, Covington, JJ., and Dowd, Sp.J., concur; Welliver, J., dissents in separate opinion filed. Rendlen, J., not sitting.

(Filed May 25, 1989)

SUPREME COURT OF MISSOURI
EN BANC

No. 71628

FREDERICK & JOSEPHINE HACKMAN,
Appellants,

v.

DIRECTOR OF REVENUE, STATE OF MISSOURI,
Respondent.

DISSENTING OPINION

Being unable to understand either the political or legal urgency for rushing into this mass refund of taxes, I have no choice but to respectfully dissent.

The principal opinion correctly and appropriately states that all parties conceded that when the U.S. Supreme Court decided Davis v. Michigan, ... U.S. ....., 109 S.Ct. 1500 (1989), it held that Michigan's scheme of exempting from taxation state retirement benefits while taxing federal retirement benefits violated and was in conflict with 4 U.S.C. § 111. All parties involved also concede that the *Davis* holding would be equally applicable to the Missouri taxing statute and that if *Davis* were to be applied retroactively, that a refund could be made under §§ 143.791 and 143.801.[1]

The principal opinion begins by stating that "we face two issues: first, whether Missouri's exemption . . . violates principles of intergovernmental tax immunity;

1. All references are to RSMo 1986 unless noted.

second, under what circumstances, federal retirees . . . may recover a refund." Hackman v. Director of Revenue, [No. 71628, decided May 25, 1989], slip op. at 2. The principal opinion then holds (as all parties had conceded) that "under the teachings of *Davis* Missouri's income tax scheme violates principles of intergovernmental tax immunity," and, "that appellants herein are entitled to a refund to the extent such refund is permitted by § 143.801." *Id.*

It is respectfully submitted that from this point on the principal opinion attempts to reason to this pre-conceived result. This I believe to be the major flaw of the principal opinion. Instead of making the "quantum leap" to the conclusion that we have a statute under which we *could* order the tax refund, which I concede to be true, we should carefully examine *Davis*, other legal precedents, federal and state, and from them reason to the wisest, fairest and most just legal solution to the problem.

I

Before examining the law to determine whether a decision to refund or not to refund is mandated by law and precedent, I would briefly look at the majority opinion and the authorities upon which it purports to rely. The majority opinion would appear to place its principal reliance for the proposition that we should first look to the Missouri statutory and case law on Nat'l. Can Corp. v. Dept. of Revenue, 109 Wash.2d 878, 749 P.2d 1286 (1988).

The majority opinion states; "[b]efore reaching the issue of retroactive/prospective application, however, a threshold inquiry is necessary." *Hackman*, ... S.W.2d

at ....., slip op. at 6, and then cites *National Can;* "[i]n order to reach the retroactivity issue, this court must first decide if . . . state statutory law or state case law mandates refunds of taxes paid prior to the Supreme Court's . . . decision. If this state's tax refund statutes . . . apply, then all other issues are irrelevant." *National Can, supra,* 109 Wash.2d at 880, 749 P.2d at 1287.

A careful reading of *National Can* reveals to the reader that the statement taken from *National Can* has no relationship to the decision of the case and that the statement is made by the Washington Court without citation of either origin or authority. *Id.*

On the same page from which the principal opinion takes the quote, the Washington Court states:

> The decisive issues before this court are whether state law mandates refunds, and if not, whether this is an appropriate case for prospective application. We hold state law does not require refunds, and prospective application is appropriate.
>
> . . . .
>
> Washington Case law does not support the proposition that tax refunds are always mandated when a statutory scheme is found to be unconstitutional.

Id.

On the following page, the Washington Court states:

> The threshold factor necessary for prospective application is a finding that the *Tyler* decision established a new principle of law overruling past precedent on which litigants may have relied.

Id. Nat'l Can, supra, 109 Wash.2d at 882, 749 P.2d at 1288, *citing* Chevron v. Huson, 404 U.S. 97, 106 (1971).

After pursuing the *Chevron* analysis, the Washington Court concludes: "[h]aving weighed the equities in this case, we conclude that pure prospective application from the date of the United States Supreme Court *Tyler* decision is appropriate, and appellant's claims for refunds before June 23, 1987 are denied." *Nat'l Can, supra,* 109 Wash.2d at 985, 749 P.2d at 1295.

Viewed in its entirety, *National Can* would appear to be one of the leading authorities in the nation supporting the Administrative Hearing Commission's denial of refunds.

If, instead of starting with a pre-conceived result, we start with the cause of the problem, the *Davis* decision, and reason from that point, we will find no difficulty in arriving at the correct, fair and just solution to the problem.

II

Davis v. Michigan

My understanding of the law suggests that this holding creates a new principle of law and a situation where we should look to what is said in *Davis* and what is held in other federal decisions to find our answer as to what should be done to solve the problem created by *Davis*. If we conclude that under the federal law the *Davis* holding should be applied retroactively, only then should we examine our Missouri law as to how to apply the holding retroactively. If we find that the federal holding should be applied prospectively only, no further inquiry is required.

It is important to distinguish between what *Davis* did, and what it did not do. *Davis* held that 4 U.S.C.

§ 111 applied to federal pensioners. *Davis* held that as a result of this construction being given to 4 U.S.C. § 111, a mandate of equal treatment was called for. *Davis* said:

> We have recognized in cases involving invalid classifications in the distribution of government benefits, that the appropriate remedy "is a mandate of equal treatment, a result that can be achieved by withdrawal of the benefits from the favored class as well as by extension of benefits to the excluded class."
>
> In this case, appellant's claim could be resolved either by extending the tax exemption to retired federal employees (or all retired employees), or by eliminating the exemption for retired state and local employees.

Davis, supra, at 1509 (emphasis in original) (citations omitted).

Davis held that the Michigan courts would be in the best position to determine how to comply with the mandate of equal treatment. As for Missouri, the General Assembly has fully complied with the mandate of equal treatment by enacting H.B. 674, which brings equality into the taxing of appellants and the other taxpayers of Missouri:

> [T]he total amount of all annuities, pensions, or retirement allowances above the amount of six thousand dollars annually provided by any law of this state, the United States, or any other state to any person except as provided in subsection 4 of this section, shall be subject to tax under the provisions of chapter 143, RSMo, in the same manner, to the same extent and under the same conditions as any

other taxable income received by the person receiving it.

C.S. No. 2 to S.S. H.C.S. H.B. 674, 85th Leg. (1989).

We should also remind ourselves that no federal pensioner is being required to pay the tax for tax year 1988 following the March 28, 1989, decision in *Davis*.

Davis did not require the retroactive application of its holding. *Davis* did not call for the refund of any of the money that Michigan had collected, and we assume already appropriated. The majority opinion suggests the reason for the Court failing to address and speak to the retroactive application was due to Michigan conceding it owed refunds. I respectfully submit that Michigan's concession that they would refund the tax if the tax were held to be "invalid" was unnecessary, ill-advised, and premature.

Let us assume that the Court had not spoken, but instead Congress on March 28, 1989, amended 4 U.S.C. § 111 to make it applicable to federal pensioners utilizing the same words used by the *Davis* court. Would anyone seriously contend that the retirees would be entitled to a refund? I submit that they would not. Two facts cause us to even consider the retroactive-prospective question. First, that it was the mere fact that it was a Court decision as opposed to a legislative enactment, and second, and more importantly I suggest, Michigan's unnecessary, ill-advised and premature concession that refunds were due.

Davis on its face indicates that the Supreme Court was not operating in a vacuum when it made its decision. The Court recognized that *Davis* was a problem confronting fourteen other states. *Davis, supra,* at 1511,

(Stevens, J. dissenting). The briefing for our case indicates there are at least twenty-one states.[2] It was in this background and with this understanding that *Davis* suggested; "that the appropriate remedy 'is a mandate of equal treatment, a result that can be achieved by withdrawal of the benefits from the favored class as well as by extension of benefits to the excluded class.' " *Id.* at 1509 (emphasis in original) (citations omitted).

The *Davis* court continued by saying that in the Michigan case, a case just like our own: "appellant's claim could be resolved either by extending the tax exemption to retired federal employees (or all retired employees), or by eliminating the exemption for retired state and local employees." *Id.*

There was no reason for Michigan's very foolish and expensive concession that they would refund. Having been afforded, as we have, additional time for more careful reading and study of *Davis*, our walking into the same trap is, I believe, inexcusable. The *Davis* court's guidance and our own legislative response made by the Missouri legislature alone should dispose of the matter.

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2. *See*, Ala.Code §§ 36-27-28 and 40-18-19 (Supp. 1988); Ariz.Rev.Stat.Ann. § 43-1022 (Supp. 1988); Colo.Rev.Stat. §§ 39-22-104(4)(f) and (g) (Supp. 1988); Ga.Code Ann. § 48-7-27(a)(4)(A) (Supp. 1988); Iowa Code Ann. § 9713.39 (West 1988); Kan.Stat.Ann. § 74-4923(b) (1985); Ky.Rev.Stat.Ann. § 16.690 (Michie/Bobbs-Merrill Supp. 1988); La.R.S. 42:545, 47:44.1 (Supp. 1989); Md.Tax-Gen.Code Ann. § 10-207(o) (1988); Miss.Code Ann. § 21-29-51 (1972); Mont.Code Ann. § 15-30- 111(2)(c) (1987); N.M.Stat.Ann. § 10-11-135 (1978); N.Y.Tax Law § 612(c)(3) (McKinney 1987); N.C.Gen.Stat. §§ 105-141(b)(13) and (14) (1985); Ore.Rev.Stat. §§ 316.680(1)(c) and (d) (1987); S.C.Code §§ 12-7-435(a), (d), (e) (Supp. 1988); Utah Code Ann. § 49-1-608 (1989); Va.Code § 58.1-322(C)(3) (Supp. 1988); W.Va.Code §§ 11-21-12(c)(5) and (6) (Supp. 1988); Wis.Stat. § 71.03(2)(d) (Supp. 1988).

III

Retrospective Application of Davis

Assuming that we conclude that it is necessary to examine the question of retroactive or prospective application of *Davis*, all parties agreed that the test for so determining is found in Chevron v. Huson, 404 U.S. 97 (1971). This Court has adopted and approved the *Chevron* test in Summers v. Summers, 701 S.W.2d 720 (Mo. banc 1985). *Chevron* states:

> First, the decision to be applied nonretroactively must establish a new principle of law, either by overruling clear past precedent on which litigants may have relied or by deciding an issue of first impression whose resolution was not clearly foreshadowed. Second, it has been stressed that "we must . . . weigh the merits and demerits in each case by looking to the prior history of the rule in question, its purpose and effect, and whether retrospective operation will further or retard its operation." Finally, we have weighed the inequity imposed by retroactive application for "[w]here a decision of this Court could produce substantial inequitable results if applied retroactively, there is ample basis in our cases for avoiding the 'injustice or hardship' by holding of nonretroactivity."

Chevron, supra, at 106-07 (citations omitted).

It cannot be disputed that *Davis* represents both a new principle of law and a case of first impression. The *Davis* opinion itself has spelled out in detail the equality required, and by passage of H.B. 674 we have already attained that equality. Missouri does not hinder the application of the new rule.

All that remains is consideration of the third prong of *Chevron,* that of weighing the equities between retro-

active and prospective application of the new principle of law. In so doing, we must keep in mind that we are not dealing with "imposition of a tax" where the appellant is pitted against his government, but rather a refund case where the appellant taxpayer is pitted against his fellow taxpayers. The question to be weighed is: Shall we impose upon either a select group of taxpayers or upon all taxpayers in general the burden of abating and refunding three years of taxes for the group represented by appellant? The question to be weighed in a state struggling to fund generally accepted and needed state services is: Shall education, health, law enforcement, and other state services be required to step aside while the state goes through the exercise of abating and refunding taxes to this select group? Exercising this abatement and refund process cannot and will not add anything to the implementation of the new principle of law announced in *Davis*, and, I do not believe that the General Assembly ever contemplated anything more by our refund statutes, §§ 143.791 and 143.801, than that taxes "illegally assessed" could be refunded. *Davis* made no holding that the taxes here in question were "illegally assessed or imposed." These taxes were legal in all of the twenty-one states involved until the Court's announcement of the new principle of law in *Davis*.

Davis, by giving the directions it gave, expressly stated that retroactive application was not necessary. On the facts before us, no compelling reason for abatement and refund is shown. All the factors of the *Chevron* test are fully met. The new principle of law announced in *Davis* requires and should be given only prospective application.

The decision of the Commission should be affirmed.

Warren D. Welliver, Judge

(Received May 1, 1989)

BEFORE THE
ADMINISTRATIVE HEARING COMMISSION
STATE OF MISSOURI

Case No. RI-89-0630

FREDERICK & JOSEPHINE HACKMAN,
Petitioners,

vs.

DIRECTOR OF REVENUE,
STATE OF MISSOURI,
Respondent.

STATEMENT OF THE CASE, FINDINGS OF FACT, CONCLUSIONS OF LAW AND DECISION

Statement of the Case

Frederick and Josephine Hackman, Petitioners, filed a claim for refund with the Director of Revenue, Respondent, seeking the return of state income taxes for 1985, 1986, 1987 and 1988, on the grounds that the taxes were collected pursuant to an unconstitutional statute. Respondent denied the refund claim on April 24, 1989. Petitioners filed a complaint with this Commission on the same day, seeking a determination that Respondent had erroneously denied the refund claim.

Pursuant to Rule 1 CSR 15-3.150(1) and § 536.073.2 (2), RSMo 1986, the parties waived a hearing and moved that this matter be summarily decided on the basis of the record before this Commission. Thomas R. Schwarz, Jr., of Jefferson City, Missouri, and P. Terence Crebs, of St.

Louis, Missouri, represented Petitioners. Randy Bakewell, Respondent's acting general counsel, represented Respondent.

Findings of Fact

The record in this matter consists of the pleadings—Petitioners' complaint and Respondent's answer—and a stipulation of facts with attached exhibits. Although the stipulation was jointly submitted, the Petitioners' objected to each and every included item as being immaterial and irrelevant. We agree. The stipulation and the attached exhibits concerned only the anticipated negative effect of Missouri's granting Petitioners' refund claim and, presumably, many more like it. Such matters, while certainly of great public concern, are irrelevant to the issue before this Commission: whether or not on the facts before us, the Petitioners overpaid their Missouri income tax for certain years and are therefore entitled to a refund of the amount overpaid.[1] Only the pleadings address that issue and our findings of fact are based solely thereon.

Based on the uncontroverted facts in the record before this Commission, we find:

1. Petitioners filed their Missouri combined individual tax returns and paid the taxes shown thereon for 1985 through 1988.

2. Pursuant to § 143.121, RSMo, they began the computation of Missouri adjusted gross income with the

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1. This Commission is powerless to consider the question which the stipulation and exhibits address, namely, whether public policy favors a refund in cases of this sort. The General Assembly has already determined that policy and has directed that "an overpayment of income tax . . . shall be refunded if it exceeds one dollar." Section 143.781.1, RSMo 1986. Where a taxpayer shows an overpayment before this Commission, we have no discretion and can only apply the law.

amount they reported as federal adjusted gross income. Included in that amount were certain pension benefits which Petitioners had received from the U.S. government as a consequence of military services rendered to the federal government.

3. The Petitioners filed refund claims for the years at issue. They asserted that the Missouri tax system, insofar as it exempted the income of state and local employees from income tax, was unconstitutionally applied to their pension benefits. Therefore, they proposed to exclude the U.S. military retirement benefits from Missouri adjusted gross income.

4. The refunds claimed were $498 for 1985; $669 for 1986; $614 for 1987; and $536 for 1988.

5. The Petitioners also proposed that they be granted interest on the refunds at the statutory rate.

6. On April 24, 1989, Respondent's authorized agent denied the Petitioners' refund claims. The Petitioners protested that denial to Respondent pursuant to § 143.841, RSMo. On April 24, 1989, Respondent denied the refund claims.

Conclusions of Law

I

The Petitioners request the refund of taxes collected under an allegedly unconstitutional statute, relying upon the recent decision of the United States Supreme Court, *Davis v. Michigan Department of the Treasury*, ... U.S. ....., 57 U.S.L.W. 4389 (March 28, 1989). Respondent contends, first, that *Davis* is not applicable to this case because the benefits paid Petitioners resulted from federal military service rather than federal civil service as in

Davis. Alternatively, he argues that if *Davis* does apply to Missouri, it should only be applied prospectively.

Section 143.011, RSMo 1986,[2] imposes a tax "for every taxable year on the Missouri taxable income of every resident." Section 143.111 provides that "[t]he Missouri taxable income of a resident shall be his Missouri adjusted gross income less: (1) either: the Missouri standard deduction or the Missouri itemized deduction, (2) the Missouri deduction for personal exemptions, (3) the Missouri deduction for dependency exemptions, (4) the deduction for federal income taxes provided in section 143.-171." Missouri adjusted gross income, in turn, is defined in § 143.121 as federal adjusted gross income with certain positive and negative modifications set out in § 143.121.

Section 143.121.2 provides for the addition to federal adjusted gross income of (1) refunds of previously-deducted, prior-year federal taxes, and (2) interest on non-Missouri governmental obligations. Section 143.121.3, in addition to certain corrections necessitated by the reform in the state income tax in the early 1970s, provides for subtraction of interest on obligations of the United States, as well as both trust distributions and refunds of prior year state income tax to the extent included in federal adjusted gross income, from federal adjusted gross income. Sections 143.121.4 and .5 provide for modifications necessary in the cases of fiduciaries and partnerships. Unlike the Michigan statute at issue in *Davis*, none of these modifications refer to pensions of any governmental retirees, local, state or federal.

Missouri state and local retirement benefits *are* generally exempt from the Missouri income tax; however,

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2. All references to the Revised Statutes of Missouri, unless otherwise indicated, are to the 1986 edition.

the exemption provisions are in the organic law of each separate retirement system. Thus, not subject to the state income tax are police and fire pensions, §§ 86.190, 86.353, 86.493, 87.365; pensions of the Missouri Highway Patrol and Department of Highways and Transportation, § 104.-250; pensions of state elected officials and state merit system employees, § 104.540; pensions of officers and employees of state political subdivisions, § 70.755; and pensions of teachers and school employees, § 169.587. These provisions encompass almost all state and local governmental retirement benefits. No similar provision exists in Missouri law for the benefit of federal retirees.

The Public Salary Tax Act of 1939, codified as amended at 4 U.S.C. § 111, provides in pertinent part:

> The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States . . . by a duly constituted taxing authority having jurisdiction, if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation.

The United States Supreme Court construed this statute in *Davis* as prohibiting state taxation of federal retirement benefits where state retirees are exempt from the state tax. The Petitioners now ask this Commission to apply the rule of *Davis* to Missouri's income tax statute. However, the Petitioners seek that which this Commission may not do.

This Commission is a quasi-judicial, administrative tribunal. It is a creature of statute, created by the General Assembly to wield limited powers in a narrow sphere. Emphatically, this Commission is not a court. Therefore, we are not empowered to declare a law of this state un-

constitutional. *City of Joplin v. Industrial Commission of Missouri,* 329 S.W.2d 687 (Mo. banc 1959); *State Tax Commission v. Administrative Hearing Commission,* 641 S.W.2d 69 (Mo. banc 1982). Petitioners' refund claim squarely, and unavoidably, presents a question of constitutional law under the Supremacy Clause. U.S. Const., Art. VI, cl. 2. Therefore, because we cannot determine the constitutionality of state statutes, we must presume existing law to be constitutional and apply it to Petitioners.

In another case, *Community Federal Savings & Loan Association v. Director of Revenue,* Case No. RV-83-0061 [2 Mo.] St. Tax Rep. (CCH) Para. 201-100 (Mo. Admin. Comm'n, July 20, 1987), this Commission did determine whether or not taxes collected pursuant to an unconstitutional statute were an "overpayment" and should be refunded to the taxpayer. However, in that case, *a circuit court* had declared the statute at issue to be unconstitutional. That case came before this Commission in a markedly different stance than did the present matter. The Petitioners in this case have not sought a declaratory judgment, but went directly to the Director of Revenue and asked for a refund on the strength of *Davis.* Neither the Respondent nor this Commission may declare a law of this state to be unconstitutional. By failing to first obtain a declaratory judgment, the Petitioners have rendered unattainable the very relief they seek.

II

The Petitioners also seek litigation expenses pursuant to § 136.315.2. That section provides, in pertinent part, that "[w]hen a party prevails . . . the court or administrative hearing commission may award the party reasonable litigation expenses if it finds that the position of the state was vexatious or was not substantially justified." "Pre-

vail" is defined as "disposition . . . which is favorable on all or substantially all issues." The Petitioners have not prevailed; therefore, they are ineligible for an award under § 136.315.

Decision

We find that because Petitioners' claim for a refund turns on a question of constitutional law, it is beyond this Commission's jurisdiction; therefore, this Commission decides for Respondent.

Wherefore, it is hereby ordered that Petitioners' complaint be dismissed from this Commission's docket this 1 day of May, 1989.

/s/ Paul M. Spinden
Paul M. Spinden
Commissioner

89-I-8

MISSOURI DEPARTMENT OF REVENUE

FREDERICK AND JOSEPHINE HACKMAN, PROTEST OF CLAIMS FOR REFUND YEARS: 1985, 1986, 1987 and 1988

INDIVIDUAL INCOME TAX
Final Decision

FINDINGS OF FACT

The Taxpayers duly filed their Missouri combined individual income tax returns and paid the taxes shown thereon for the years at issue. Pursuant to § 143.121, they began the computation of Missouri adjusted gross income with the amount they reported as federal adjusted gross income. Included in that amount were certain pension benefits which Mr. Hackman received from the U.S. government. These benefits were paid to him as a consequence of military services rendered to the government.

On or about March 28, 1989, the U.S. Supreme Court handed down its opinion in the case of *Paul S. Davis v. Michigan Department of Treasury,* 57 U.S.L.W. 4389 (March 28, 1989). The Court held that it was improper for a state to exempt the pension income of its own state and local employees from its income tax while taxing that of federal employees. In reaching its conclusion, the Court relied on 4 U.S.C. 111 and principles of intergovernmental tax immunity.

The State of Missouri exempts most state and local pensions from income tax. The retirement benefits of Missouri state employees were given a statutory exemption in 1957. But the retirement benefits of all other employees, including U.S. military retirees, are subject to tax.

The Taxpayers filed timely refund claims for the years at issue. They asserted that the Missouri tax system, insofar as it exempted the income of state and local employees from income tax, was unconstitutionally applied to their pension benefits. Therefore, they proposed to exclude the U.S. military retirement from Missouri adjusted gross income.

The refunds claimed were as follows:

1985	$498.00
1986	$669.00
1987	$614.00
1988	$536.00

The Taxpayers also proposed that they be granted interest on the refunds at the statutory rate.

On or about April 24, 1989, an agent of the Director of Revenue denied the Taxpayer' refund claims. Taxpayers duly protested that denial to the Director of Revenue pursuant to § 143.841.

BASIS OF DECISION

First, it should be noted that *Davis* only addressed U.S. civil service employees and not military retirees. While it seems probable that *Davis* is applicable to the circumstances in this case, the Director must presume that the Missouri statutes are constitutional.

Further, even if it is found that *Davis* is applicable, no refunds or other relief is due.

Article I, § 13 of the Missouri Constitution prohibits retroactive laws. The Missouri Supreme Court has held that this results in income tax liability being fixed as it accrues. See *Graham Paper Company v. Gehner,* 59 S.W.

2d 49 (Mo. banc 1933). In this case, the U.S. Supreme Court's mandate was not issuable until April 22, 1989. But the liability for all years had vested prior to January 1, 1989 (This defeats any argument based on the assessment provision of Mo. Rev. Stat. Chapter 143 that liability for calendar year 1988 did not exist until April 15 (or 17), 1989).

While in the past Missouri courts generally applied their decisions retroactively, the Missouri Supreme Court adopted the modern *Chevron Oil Co. v. Huson,* 404 U.S. 96, 106-107 (1971) approach in *Sumners v. Sumners,* 701 S.W.2d 720 (Mo. banc 1985). The *Chevron* approach adopted by the Missouri Supreme Court in *Sumners* was the same test applied in *National Can* to hold that *Tyler Pipe* is applied prospectively in Washington. It is the Director's view, based on the Missouri Supreme Court decision in *Sumners,* that if the *Chevron* issue is properly raised in a tax case in Missouri, the Missouri Supreme Court will apply the three part *Chevron* test.

This test was set out by the Washington Supreme Court in *National Can,* 749 P.2d at 1288, as follows:

> Courts must (1) determine whether the decision establishes a new principle of law either by overruling clear past precedent on which litigants may have relied, or by deciding an issue of first impression whose resolution was not clearly foreshadowed; (2) weigh the merits and demerits in each case by looking to the prior history of the rule in questions, its purpose and effect and whether retrospective operation will further or retard its operation; and (3) weigh the inequity imposed by retroactive application.

The First Factor Under the Chevron Test:

The first factor under the *Chevron* test is whether *Davis* establishes a new principle of law by either overruling clear past precedent, or by deciding an issue of first impression whose resolution was not clearly foreshadowed.

Missouri state and local pension statutes have provided for state income tax exemptions beginning with the police pension law amendments of 1929 (currently in § 86.190). Additional exemptions have been adopted from time to time since that early provision, and most of them were adopted after enactment in 1939 of 4 U.S.C. § 111. In addition, approximately nineteen states currently provide for exemption of some state pensions while taxing some or all federal pensions. We have found no decisions at any level which invalidated any of such exemptions prior to the United States Supreme Court opinion of March 28, 1989 in *Davis*. Indeed, the dissent in *Davis* notes Missouri and many other states have maintained such a system for many years. It is therefore our view that *Davis* was not foreshadowed within the meaning of the first *Chevron* factor.

The Second Factor Under the Chevron Test—Will Retroactive Operation Further or Retard the Operation of Davis?

At issue in *Davis* was the relationship between the states and the federal government; as with the Commerce Clause question in *Tyler Pipe Industries, Inc. v. Washington Department of Revenue*, ... U.S. ....., 107 S.Ct. 2810 -1987), retroactive application of *Davis* will not undo prior discrimination.

The Third Chevron Factor—Is Retroactive Application Inequitable?

The prospective application of *Davis* would deprive federal pensioners of refunds of state income taxes paid during all periods open under the Missouri income tax refund statute of limitations. On the other hand, federal pensioners have been treated in the same manner by Missouri as all private pensioners, and some state pensioners.

Refunds to federal pensioners would create difficult hardships for Missouri and its political subdivisions. The United States Supreme Court has recognized hardships to state political subdivisions as a basis for prospective application, *Cipriano v. Houma,* 395 U.S. 701 (1969), particularly where state funds had already been spent prior to the decision, *Lemon v. Kurtzman,* 411 U.S. 192 (1973). The hardship to Missouri is evident from the fact that the Commissioner of Administration has recently suggested that the total revenues loss from *Davis* (including refunds) would be approximately $192 million.

Furthermore, Missouri has for many years relied on its ability to generate revenue from the income tax on federal and other pensions. This is a clear element of equity favoring the state. In *Ashland v. Rose,* 350 S.E.2d 531, 537 (W. Va. S.Ct. 1986), *app. dismissed,* 107 S.Ct. 1949 (1987), the Court stated that, "We believe, therefore, that the reliance of the State of West Virginia on a presumptively valid tax outweighs any injury that may be sustained by Ashland on account of our holding of prospectivity."

We therefore believe that the third arm of *Chevron* is satisfied by the prospective operation of *Davis.* Retroactive relief should be denied.

Further, the General Assembly may decline to appropriate funds for refunds. *See, State ex Inf. Danforth v. Merrill,* 530 S.W.2d 209 (Mo. banc 1975).

DECISION

It is the Final Decision of the Director of Revenue upon reconsideration that the Denial of Refund Claims are correct and remain outstanding.

If you were adversely affected by this decision, you may appeal to the Administrative Hearing Commission. To appeal, you must file a petition with the Administrative Hearing Commission within thirty days after the date this decision was mailed, or the date it was delivered, whichever date was earlier. If any such petition is sent by registered mail, it will be deemed filed on the date it is mailed; if it is sent by any method other than registered mail, it will be deemed filed on the date it is received by the Commission.

/s/ Duane Benton
Duane Benton
Director of Revenue

/s/ Randy Bakewell
Randy Bakewell
Acting General Counsel

Date: April 24, 1989.

(Received August 22, 1989)

BEFORE THE
ADMINISTRATIVE HEARING COMMISSION
STATE OF MISSOURI

Case No. RI-89-0630

FREDERICK & JOSEPHINE HACKMAN,
Petitioners,

vs.

DIRECTOR OF REVENUE,
STATE OF MISSOURI,
Respondent.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

Frederick and Josephine Hackman, Petitioners, filed a claim for refund with the Director of Revenue, Respondent, seeking the return of state income taxes for 1985, 1986, 1987 and 1988, on the grounds that the taxes were collected pursuant to an unconstitutional statute. Respondent denied the refund claim on April 24, 1989. This Commission dismissed the Petitioners' claim on the same day because we lacked jurisdiction to consider a purely constitutional claim; the effect was to uphold the Respondent's decision. The Missouri Supreme Court reversed our decision, declared Missouri's income tax statute to be unconstitutional as applied to Petitioners, and remanded the cause to this Commission for a determination of whether or not a refund is due. *Hackman v. Director of Revenue,* 771 S.W.2d 77 (banc 1989).

Pursuant to Rule 1 CSR 15-3.150(1) and § 536.073.2 (2), RSMo 1986, the parties waived a hearing and moved that this matter be decided on the basis of the record before this Commission. Attorney at Law Thomas R. Schwarz, Jr., of Jefferson City, Missouri, represented Petitioners. George Cox, Respondent's Senior Attorney, represented Respondent.

Findings of Fact

The record in this matter consists of the pleadings, two stipulations of fact, one of which was accompanied by several exhibits, and an affidavit of Petitioner Frederick Hackman. Based on the uncontroverted facts in the record before this Commission, we find:

1. Petitioners filed their Missouri combined individual tax returns and paid the taxes shown thereon for 1985 through 1988. The Petitioners filed their 1985 return on April 15, 1986, by depositing it into the United States Mail, postage prepaid, on that date.

2. Pursuant to § 143.121, RSMo 1986, they began the computation of Missouri adjusted gross income with the amount they reported as federal adjusted gross income. Included in that amount were certain pension benefits which Petitioners had received from the United States government as a consequence of military services rendered.

3. The Petitioners filed refund claims for the years at issue. The claim relating to 1985 was filed on April 10, 1989. They asserted that the Missouri tax system, insofar as it exempted the income of state and local employees from income tax, was unconstitutionally applied to their pension benefits. Therefore, they proposed to ex-

clude the federal military retirement benefits from Missouri adjusted gross income.

4. The refunds claimed were $498 for 1985; $669 for 1986; $614 for 1987; and $536 for 1988.

5. The Petitioners also proposed that they be granted interest on the refunds at the statutory rate.

Conclusions of Law

I

The Petitioners request the refund of taxes collected under an unconstitutional statute, relying upon the recent decision of the United States Supreme Court, *Davis v. Michigan Department of the Treasury,* ..... U.S. ....., 109 S.Ct. 1500, 103 L.Ed.2d 891 (1989). The applicability of that decision to Missouri's income tax statutes was confirmed by the Missouri Supreme Court. *Hackman v. Director of Revenue,* 771 S.W.2d 77 (en banc 1989).

Section 143.781.1, RSMo 1986,[1] authorizes the Respondent to refund overpayments of tax "within the applicable period of limitations." That period is set out in § 143.801.1:

> A claim for credit or refund for overpayment of any tax imposed by sections 143.011 to 143.996 shall be filed by the taxpayer within three years from the time the return was filed or two years from the time the tax was paid, whichever of such periods expires the later . . . . No credit or refund shall be allowed or made after the expiration of the period of limitation prescribed in this subsection for the filing of a claim

1. All references herein to the Revised Statutes of Missouri are to the revision of 1986 unless otherwise noted.

for credit or refund, unless a claim for credit or refund is filed by the taxpayer within such period.

We have previously determined that the time limitations imposed by this provision contemplate actual *calendar years. Hamacher v. Director of Revenue,* Case No. RI-89-0968, [2 Mo.] St. Tax Rep. (CCH) Para. ..... (Mo. Admin. Hearing Comm'n, 1989). The Petitioners filed their return for 1985—and paid the amount shown to be due thereon—on April 15, 1986. They filed their claim for refund on April 10, 1989, five days prior to the expiration of the lawful filing period. Therefore, the claim was timely filed and a refund is due to the Petitioners for the Missouri state income tax paid on the federal pension benefits received in 1985 and for the corresponding amounts paid on the years 1986, 1987 and 1988.

Decision

We find that the Petitioners have shown that Respondent erroneously denied their claim for refund because their claim was timely filed; therefore, we conclude that Respondent's final decision was erroneous and should be set aside.

Entered this 21 day of August, 1989.

/s/ Paul M. Spinden
Paul M. Spinden
Commissioner

PMS/kat/jrh